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Commentary: AB 182 would help taxpayers monitor bonds

By Michelle Steel

Most people have the good sense not to take out a loan that will cost them 20 times more than what they initially borrowed.

But that is not true for some local governments. That is why I supported the passage of Assembly Bill 182, which places limits on risky borrowing by local governments. Now it's up to Gov. Jerry Brown to sign it.

Bonds are a popular tool for state and local government to finance projects. Like a home loan, bonds are typically financed for about 30 years, with the money coming from investors.

In and of itself, a bond is not the most responsible way to pay for a project.

First, the amount of money repaid over the term of the bond ends up being many times more than the original amount borrowed. On average, a current interest bond, or CIB, has a debt to principle ratio of 2 or 3 to 1, meaning the amount of principal and interest paid back over the term ends up being two or three times the amount of money initially borrowed.

Second, the life of a project, such as repairing a government building or constructing a new road, can be much shorter than the time it will take to pay off a loan. For example, a new road built with bond money may require heavy modifications because of increased traffic after only 20 years. It may even need to be scrapped and rebuilt. Yet taxpayers are forced to continue paying for the project for another decade.

The amount of money that a government entity can borrow is usually determined by the potential tax revenue available for paying back the loan. In recent years, tax revenues have decreased, lowering the amount of money that can be borrowed.

To make up for the lower borrowing capacity, some government entities have turned to more dangerous bond schemes called capital appreciation bonds, or CABs. Unlike CIBs, CABs defer principal and interest payments for up to 20 years, accruing more interest on top of the interest that is being deferred.

CABs allow government entities to borrow more money, but they also increase dramatically the long-term cost of borrowing. The debt-to-principal ratio of a CAB typically ranges from 3.5 to 1 all the way up to 23 to 1.

Recently, the Poway Unified School District approved a CAB for \$105 million. When the bond matures in 2052, the district will have to pay back \$981 million, a debt-to-principle ratio of more than 9 to 1. In San Bernardino, another district borrowed \$283,000, to be paid over 29 years. The final cost: \$6.6 million — a debt-to-principle ratio of 23 to 1!

That is why I strongly endorsed AB 182. The bill is a step in the right direction. While it doesn't prohibit expensive CABs, it at least imposes tougher restrictions on entities that would like to issue them.

These restrictions include a limit on the maximum term of CABs to no more than 25 years, and a 10-year cap on deferment of principal and interest payments. AB 182 also limits the debt-to-principle ratio to 4 to 1.

Finally, government entities interested in issuing CABs would be required to hold hearings and provide information and analysis about the true costs and structure of these bonds before approving them.

Fortunately, AB 182 has passed the Legislature and is on the governor's desk. With his signature, taxpayers would gain additional protections and more of the tools they need to make informed decisions and hold their elected officials accountable for actions that affect future generations.

Surfside resident **MICHELLE STEEL** is a member of the State Board of Equalization. She is running for the Orange County Board of Supervisors, District 2, which includes Costa Mesa, Newport Beach, Huntington Beach, Seal Beach and portions of Fountain Valley.